Osborn, Carreiro & Associates, Inc.

ACTUARIES ● CONSULTANTS ● ANALYSTS

One Union National Plaza, Suite 1690
124 West Capitol Avenue
Little Rock, Arkansas 72201
(501)376-8043 fax (501)376-7847

House Bill 1325

(With Amendment #1, April 5, 2021)
Actuarial Cost Study prepared for
Joint Committee on Public Retirement and Social Security Programs
of the Arkansas 93rd General Assembly

Provisions of the Bill

House Bill 1325 affects most of the statewide retirement systems. The exceptions are the Arkansas Judicial Retirement System (AJRS) and the closed local fire and police plans (Local Plans). We understand that the directors of the statewide systems worked together to improve the subchapter that deals with reciprocity. The primary purpose was to clarify and condense the language – for example, a couple of terms were defined more than once in the subchapter which can cause ambiguity. The secondary purpose, which is a change to current practice, was to allow each system to define the final salary used in reciprocal calculations. House Bill 1325 makes both changes.

NOTE: House Bill 1325 was given a "Do Pass" recommendation from this committee on March 15, 2021. Due to concerns, the sponsor has amended this bill with a grandfather clause regarding the use of the highest final average salary for anyone who currently has reciprocal service.

What is Reciprocity?

In general, reciprocity between systems allows the use of the service under all the systems to determine the eligibility for benefits. One economic benefit to a participant is the ability to access the early retirement options, like 28 and out. The participant that establishes reciprocity would still receive a benefit from each of the systems in which they participated but could combine all his years to meet the 28-year requirement.

An example would help explain. Here System A is the first employer and System B is the last employer.

	System A	System B
A. Years of Service	10	20
B. System Multiplier	2.0%	2.2%
C. Final Average Salary in System	$30,000	$55,000
D. Current Salary for Reciprocity	$55,000	$55,000
E. Benefit from each System (AxBxD)	$11,000	$24,200
Under House Bill 1325		
F. Benefit from each System (AxBxC)	$6,000	$24,200

The participant gets to add together their service (10 + 20 = 30), so that they are eligible for 28 and Out and can retire or go on DROP in both systems. If they went to work at System A at age 30, then they can receive five more years of benefits than they would without reciprocity. That is, they can retire at age 60 with reciprocity versus age 65 without reciprocity.
Currently, this example participant also receives an additional $5,000 per year for those extra five years. System A priced into their system that some individuals would leave after becoming vested and that they would receive $6,000 per year at age 65. Under current reciprocity, they will pay $11,000 per year beginning at age 60. This is 210% to 220% of the value established by System A.

Every example that you construct will be different. Some are not this significant, but many are even more extreme. We reviewed recent real examples that are more extreme that the one shown above. The one thing in common among all examples, is that both systems share in the cost of early retirement due to reciprocity, but the first system of employment bears a much more significant cost due to the highest salary part of the formula.

Fiscal Impact

There is not a good source of data concerning reciprocity until after the service is established and the participant retires. This makes it difficult to estimate the cost to the ongoing system. During the research for Senate Bill 5 (LOPFI) we looked at the data from the terminated vested participants for the past 2 years who had reciprocal service. We calculated that about 10% of this group retired with some reciprocal service and that the salary adjustment was an average of a 70% increase. We estimated that this resulted in extra cost to the system in the range of 0.15% to 0.30% of payroll each year. Some of the system actuaries had estimated this cost in the range of 0.4% of payroll. Based on this information and various examples we have reviewed; it is our opinion that if the systems use their own final average salary definition, they will eventually (over five to ten years) see a cost reduction equivalent to 0.25% to 0.50% of payroll.

Related Legislation

There have been several bills this session that were part of the various system's legislative package where they worked to better define the salary used within their system when reciprocity existed. Senate Bill 5 (LOPFI), Senate Bill 104 (ASHERS) and House Bill 1319 (ATRS) were all approved by this Committee. The passage of House Bill 1325 would ensure that there are no conflicts with reciprocal law and individual system law.

Sincerely,

Jody Carreiro

Jody Carreiro, EA, ASA, MAAA, FCA
Actuary

Additional Disclosures on file with BLR